COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

NEW ENGLAND TELEPHONE AND TELEGRAPH COMPANY d/b/a VERIZON (Alternative Regulation Plan - Sixth Price Cap Compliance Filing)

DTE 00-101

PETITION OF AT&T COMMUNICATIONS OF NEW ENGLAND, INC.

TO SUSPEND AND INVESTIGATE PROPOSED TARIFF

Introduction

AT&T Communications of New England, Inc. ("AT&T") petitions the Department of Telecommunications and Energy ("Department" or "DTE") to suspend and investigate the proposed tariff revisions to M.D.T.E. No. 10 filed by New England Telephone and Telegraph Company, d/b/a Verizon ("Verizon") with the Department on October 2, 2000 ("October 2 Tariff Filing"). In the absence of Department action, the tariff revisions will become effective on December 15, 2000.

Verizon's proposed tariff revisions raise a number of issues: Verizon's continued failure to demonstrate satisfaction of a price floor calculation that the Department has accepted, Verizon's treatment of new services in determining whether Verizon has satisfied the pricing rules under the price cap plan, Verizon's use of the rates and quantities of wholesale services not subject to the price cap plan to determine compliance with the pricing rules of the price cap plan, and failure to provide notice to other parties when it introduces new services and files the required support to demonstrate compliance with price floor requirements. Further discussion of each of the foregoing issues follows.

Before, however, AT&T addresses the narrow issues identified above, it is important to reference the larger context in which this filing is taking place. This filing is the last filing under the price cap plan that was put in place pursuant to the Department's May 12, 1995 decision in D.P.U. 94-50. One of the reasons that the Department established a price cap form of regulation was to provide increased pricing flexibility to the incumbent telecommunications carrier in order that it could respond to competitive pressures that were expected to develop. There was, however, no experience with real competition at the time. There was almost no competition in the intraLATA toll market before dialing parity was implemented, and there was - for all practical purposes - no local service competition.

Since that time, there has been much experience. The experience has not so much been in the development of competition as it has been in the substantial effort to put in place a set of conditions that will allow that competition to develop. Although some progress has been made, experience shows that many assumptions made when the price cap plan was put in place and during its early life will need to be revisited in light of experience. At the time that the price cap plan was put in place, the Department truncated its planned increase of retail rates to economic levels. See, D.P.U. 94-185 (May 12, 1995) at 129. See also, id. at 123, n. 79(1). Later, the Department decided that price floor requirements could be satisfied by offering the retail service at wholesale rates. As a result of these two decisions, it became possible for the incumbent to charge retail rates under the price cap plan at levels that are less than the price of the network elements competitors must purchase to offer the same retail service. Clearly, under such situations, facilities based competition evolving out of the purchase of unbundled network elements will simply not occur.

Although the glaring imbalance between the retail rates allowed under the plan and the wholesale rates that have since been established for the elements necessary to compete is not technically before the Department in this docket, it soon will be. The current price cap plan will end in August, 2001. D.P.U. 94-185 (May 12, 1995) at 271-272. The Department should establish a proceeding immediately to consider the type of price cap plan that will allow Verizon legitimate pricing flexibility while at the same time create a relationship between wholesale and retail rates that does not impose - as it now does - a price squeeze that precludes facilities based competition.

Comments and Argument

I. VERIZON'S PROPOSED RATES HAVE NOT BEEN SHOWN TO SATISFY PRICE FLOOR REQUIREMENTS.

On August 24, 2000, Verizon filed revised price floor ("August 24 Filing"), pursuant to directives in the Department's August 3, 2000, order, D.P.U./D.T.E. 94-185-E ("Price Floor Order"). In the Price Floor Order, the Department directed Verizon to make certain changes to the price floor calculations that it had filed on November 2, 1998. In filings with the Department in D.P.U./D.T.E. 94-185 on September 12, 2000, and on October 24, 2000, AT&T challenged Verizon's August 24 Filing, pointing out five separate ways in which it did not comply with the Department's Price Floor Order. (Copies of the two AT&T filings are attached hereto for the Department's convenience.)

Verizon appears to have used the same faulty methodology in the October 2 Tariff Filing as it used in its August 24 Filing in order to claim that the proposed rates here satisfy price floor requirements. See, October 2 Tariff Filing, Section B, Tab 3. As AT&T noted in its September 12 letter to the Department in D.P.U./D.T.E. 94-185, Verizon's unauthorized adjustments of intra-state revenues for purposes of calculating the retail overhead expense factor can have a material effect on the outcome of a price floor analysis. In the August 24 Filing, Verizon's unauthorized adjustments decreased the retail overhead expense factor by almost 15%, from 18.86% to 16.02%. By reducing the calculated price floor, Verizon makes it less likely that the reductions in its retail rates will violate the price floor as calculated, when - in fact - they would violate a properly calculated price floor. Indeed, Verizon's unauthorized adjustments have a material effect on the results in the present case.

Substituting 18.86% for Verizon's unauthorized 16.02% and using the same switched access rate as Verizon used in its August 24 Filing,(2) both the Baystate Non-Metropolitan Service and the Business Link Service fail a price floor analysis. Instead of "passing" a price floor analysis by $51,108, the Baystate Non-Metropolitan Service fails by approximately $20,000. Instead of "passing" a price floor analysis by $182,243, the Business Link Service fails by approximately $18,000. In short, Verizon's proposed rates should not be allowed to go into effect until it has established that its rates satisfy Department approved price floor requirements.

Moreover, the razor-thin margin by which the remaining optional calling plans purportedly "pass" the price floor analysis requires that the Department carefully consider the data and assumptions underlying Verizon's analysis. The use of unsupported and potentially inaccurate data is -- in words that have become familiar as a result of the recently reported election contest -- sufficient to "place in doubt" the outcome of Verizon's price floor analysis, given the closeness with which Verizon "passes" the price floor test as filed. For example, in addition to the above referenced unsupported change in Switched Access Rates, Verizon's price floor analysis relies on unsupported data which - on their face - appear suspect. In its October 2 Filing, Verizon shows its MTS - Business revenues as $1.4 million as compared to MTS - Business revenues of $2.7 million in its August 24 Filing. This reduction appears to be driven by an unexplained drop in minutes from 40.6 million to 25.1 million. The accuracy of projected minutes and revenues for these services has a material impact on the price floor analysis. Verizon should be required to support a price floor analysis before its new, reduced rates for potentially competitive intra-LATA toll services are allowed to go into effect.

II. VERIZON'S TREATMENT OF NEW SERVICES IN DETERMINING WHETHER VERIZON HAS SATISFIED THE PRICING RULES UNDER THE PRICE CAP PLAN NEEDS TO BE EXAMINED.

Verizon determines compliance with the pricing rules of the price cap plan by first deriving the percentage by which its revenues must decrease (if the formula requires a reduction) or the percentage by which its revenues may increase (if the formula permits an increase). Verizon then adjusts its previous year's revenues by that amount to determined its allowed amount ("Allowed Amount"). Verizon then determines whether its proposed prices produce revenues that are equal to or less than the Allowed Amount. It does so by multiplying the quantities of services sold in the preceding year by the proposed prices ("Proposed Amount") and comparing the Proposed Amount to the Allowed Amount. In Verizon's analysis, it satisfies the price cap requirements if the Proposed Amount is less than the Allowed Amount, assuming all other price rules are satisfied.

Verizon's method, therefore, relies upon an acceptable number for the quantity of services sold. For services that have been in place for many years, that quantity is reasonably estimated by the quantity in the previous year. However, for new services, especially those that have been introduced within the 12 months preceding the annual price cap compliance filing, the preceding year's quantity is not valid. Indeed it is zero for services introduced within the preceding 12 months.

Without further investigation, it is not at all clear how Verizon has treated these new services for purposes of the price cap analysis. At a minimum, Verizon should be required to demonstrate how it has done so. Until Verizon has demonstrated that its proposed rates satisfy price floor requirements, the Department should not approve them.

III. IT IS NOT CLEAR THAT VERIZON SHOULD USE THE RATES AND QUANTITIES OF WHOLESALE SERVICES NOT SUBJECT TO THE PRICE CAP PLAN TO DETERMINE THE COMPLIANCE OF SERVICES SUBJECT TO THE PLAN.

As explained above, Verizon's price floor analysis relies on a comparison of the preceding year's revenues to the proposed revenues, assuming prices change as proposed but quantities do not. When this method was initially developed, virtually all of Verizon's services were services subject to the price cap plan, i.e., either retail services or access services. Initially, therefore, the prices and quantities used in the price cap analysis were prices and quantities associated with the services that were subject to the price cap plan. With the passage of time, however, services not subject to the price cap plan are making up an ever increasing proportion of Verizon's revenues. Those services include all those offered under interconnection agreements and under Tariff 17. They include reciprocal compensation revenues, collocation revenues, conduit lease and pole attachment revenues, revenues from the sale of unbundled network elements and revenues from resale.

Verizon's October 2 Filing appears to include the revenues from all of these new services in its analysis. See, e.g., Section C, Tab 1, p. 21. For example, in addition to several million dollars from poles and conduits, Verizon appears to have included almost $92 million from local traffic termination. The rates for these services are determined in negotiated or arbitrated interconnection agreements or litigated tariffs; they are not subject to the price cap plan. Indeed, the flexibility granted to Verizon to adjust rates under the price cap plan would be entirely inappropriate for establishing the prices in interconnection agreements and wholesale tariffs.

The question, therefore, arises as to whether Verizon should be including services not subject to the price cap plan in an analysis used to determine compliance with the price cap plan. This is a question for which the implications will grow quickly over time, with the growth in Verizon's wholesale revenues. The Department should address it now before permitting rates under the price cap plan to go into effect based on revenues from services not subject to the price cap plan.

IV. VERIZON'S FAILURE TO PROVIDE NOTICE TO OTHER PARTIES WHEN IT INTRODUCES NEW SERVICES AND FILES PURPORTED SUPPORT TO DEMONSTRATE COMPLIANCE WITH PRICE FLOOR REQUIREMENTS VIOLATES THE SPIRIT, IF NOT THE LETTER OF THE DEPARTMENT 1995 PRICE CAP DECISION

In D.P.U. 94-50, the docket in which the current price cap plan was established, Verizon (then NYNEX) had argued that it should not be required to provide information demonstrating compliance with the price floor requirement unless and until another party challenges a proposed price. The Department rejected that view, stating that "NYNEX would have an unfair advantage if it could introduce services and keep those services in effect while [price floor] complaints are resolved." D.P.U. 94-185 (May 12, 1995) at 257-258.

As noted above, Verizon has filed tariffs introducing a number of new services over the past two years. With each such filing it has provided what it contends is support for price floor compliance. Verizon has not, however, served either the tariff filing or the purported support on AT&T. Accordingly, AT&T has only become aware of these new services at the time that Verizon makes its annual price cap compliance filing, after the service has already gone into effect. In the absence of a daily review of Department files by Verizon's competitors, therefore, Verizon will have achieved the unfair advantage the Department sought to prevent - introduction of new services before price floor compliance is demonstrated.

Verizon's competitors should not have to review Department files every day for the possibility that Verizon may introduce a new service with price floor implications. Verizon should be required to serve on its competitors the price floor analysis that it is required to provide them.

Conclusion

For the foregoing reasons, AT&T requests that Verizon's proposed tariff revisions be suspended and further investigated.

Respectfully submitted,

AT&T COMMUNICATIONS OF NEW ENGLAND, INC.

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1. 1 The Department stated: "The current residential dial-tone line monthly rate is $9.91, and the Company has proposed to freeze that rate, among others, until August 2001 … Under the transitional rate-restructuring, the residential dial-tone line monthly rate would have increased to the target rate of $15.00 in two additional transitional filings." Id. (citations omitted).

2. 2 In its August 24 Filing, Verizon used a Switched Access rate of 0.038325 (Exhibit, p. 2 of 3, line j), while in its October 2 Filing, it used a Switched Access rate of 0.038163 (Section B, Tab 3, p. 3 of 4, line 4). Verizon provides no support for its new Switched Access rate in the October 2 Filing.